**BEFORE THE**
**FEDERAL COMMUNICATIONS COMMISSION**

| | | |
|---|---|---|
| In the Matter of | ) | |
| | ) | |
| Consumer Federation of America, International Communications | ) | |
| Association and National Retail Federation Petition Requesting | ) | Docket No. |
| Amendment of the Commission's Rules Regarding Access Charge | ) | RM9210 |
| Reform and Price Cap Performance Review for Local Exchange Carriers | ) | |

# REPLY COMMENTS OF CONSUMERS UNION AND THE CONSUMER FEDERATION OF AMERICA

Consumers Union[1] joins with the Consumer Federation[2] in these reply comments to urge the Federal Communications Commission (FCC) to initiate a rule making to immediately implement access charge reform.

The Commission has now heard support for immediate access charge reform from all consumers of telecommunications services. To the voices of the nation's two oldest and largest groups representing small, residential consumers have been added the voices of several groups representing medium and large consumers.[3]

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[1]Consumers Union is a nonprofit membership organization chartered in 1936 under the laws of the State of New York to provide consumers with information, education and counsel about goods, services, health, and personal finance; and to initiate and cooperate with individual and group efforts to maintain and enhance the quality of life for consumers. Consumer's Union's income is solely derived from sale of *Consumer Reports*, its other publications and from noncommercial contributions, grants and fees. In addition to reports on Consumers Union's own product testing, *Consumer Reports* with approximately 4.5 million paid circulation, regularly carries articles on health, product safety, marketplace economics and legislative, judicial and regulatory actions which affect consumer welfare. Consumers Union's publications carry no advertising and receive no commercial support.

[2]Founded in 1968, the Consumer Federation of America is the nation's largest consumer advocacy group. Composed of over 250 state and local affiliates representing consumer, senior citizen, low-income, labor, farm, public power, and cooperative organizations, CFA's purpose is to represent consumer interests before the congress and the federal agencies and to assist its state and local members in their activities in their local jurisdictions.

[3]In addition to the original petitioners, International Communications Association and the National Retail Federation, the Commission has now heard from the Ad Hoc Telecommunications Users Group and the American Petroleum Institute.

Based on the evidence in this proceeding, it is clear beyond any doubt that the consuming public would benefit from an immediate reduction in access charges and that competition in the telecommunications industry will not get started without immediate reform of access charges. As long as the local exchange companies (LECs) enjoy billions of dollars of monopoly profits and pricing rules that protect their excess profits, inefficiencies and strategically misallocated costs, their primary corporate interest will be to prevent competitors from entering the market to threaten those revenues. Two years after the passage of the Telecommunications Act of 1996, they have demonstrated a remarkable ability to frustrate competition.

As the attached report by the Consumer Federation, entitled Competition in Local Telephone Market: Is the Glass 98 Percent Empty or 2 Percent Full, shows, any suggestion that the FCC can wait for developments in the marketplace to do the job of lowering access charges to the efficient, forward looking levels that would prevail in a competitive marketplace has been laid to rest by the evidence in this proceeding.

## THE CURRENT STATE OF COMPETITION

Rather than enjoying a vigorously competitive marketplace as the LECs claim, consumers still face a market that is monopolized by the incumbent LECs and immune to the market forces that would deliver the competitive benefits that the Telecommunications Act of 1996 promised. The simple, inescapable fact is that there is not now effective competition in access service.

- Even if we accept their overblown claims about business lost to competitors, the four LECs who have made data available retain a 98 percent market share.

- Moreover, the LEC share of facilities-based competition, which is all that counts for access charge reform and in the long run what

counts in the marketplace, is even higher, over 99 percent.

- Finally, it turns out that LECs have not even "lost" anything. For all the complaining about competitive incursions into their business, the Baby Bells have added over four times as many lines as competitors since the passage of the 1996 Telecom Act.

- Many claim to have added lines and revenues at record levels in 1997.

In the new era of common sense regulation advocated by the Commission, perhaps the most bedrock common sense notion that Americans have about their marketplace economy is that companies with a 98 or 99 percent market share do not face effective competition.

## PROSPECTS FOR COMPETITION

The simple, inescapable fact is that the regulatory structure that the FCC had hoped would foster competition under the 1996 Act has been severely damaged, if not destroyed, by the unrelenting resistance of LECs to local competition in the courts, the marketplace, and the regulatory arena. Since the FCC acted in the access reform docket, the market opening process has suffered a series of major setbacks including

- FCC's pricing rules vacated,

- cost-based UNE pricing reopened in many states by the 8th Circuit ruling,

- FCC's section 251 role restricted,

- scope of the FCC's 271 review limited,

- UNE platform undermined by the 8th Circuit's recombination ruling

- the LEC refusal to provide shared transport,

- RBOC restrictions invalidated,

- o Number Portability implementation schedule delayed,
- o Operational Support Systems have failed to develop,
- o section 271 applications have become weaker, not stronger,
- o section 271 found unconstitutional by a lower court.

The commitment of the LECs to complying with section 271 of the 1996 Act is subject to serious doubt. The companies that led the charge in attacking the statute have said different things in different places at roughly the same time -- professing to accept and support section 271 before some courts and regulatory commissions while simultaneously challenging it in others.

Even the companies who have claimed to be most committed to opening their markets jumped on the bandwagon that sought to overturn the statute. It is ironic and troubling to hear corporate officers claim that their fiduciary responsibility to stockholders requires them to participate in the law suits seeking to overturn the Act, but they really want to comply with it. It is clear that their overarching responsibility is to defending their monopoly revenues as best they can.

We believe that the FCC has a fiduciary responsibility to the public, to lower prices it has repeatedly and loudly proclaimed are above cost, uneconomic and incompatible with a competitive marketplace. The regulatory agency charged with protecting the public must be just as vigorous in its defense of the public interest as the corporation have been in defense of their private interests. The only way that the FCC can immediately and effectively do that is to lower access charges.

While we encourage and support the FCC in its efforts to open markets under the 1996 Act, access charge reform is not dependent on the 1996 Act. It need not, and, in light of the

actions of the LECs who are resisting opening their markets are every turn, it should not wait for competition to succeed or fail under the Act. Access charge reform should begin now.

## THE LEGAL BASIS OF ACCESS CHARGE REFORM

Whenever the LECs are confronted with the prospect of having their revenue streams reduced, no matter what proceeding at the state or federal level, they insist that their constitutional rights of property are about to be violated.

- Since this legal challenge is inevitable, we urge the FCC to take aggressive action to lower consumers bills now and defend that decision in the courts. Put the money in the people's pockets and let the LECs try to take it out through court cases. We are convinced they will fail and that state and federal regulators should not delay competition over the issue of embedded costs.

The version of the regulatory compact between stockholders and ratepayers that LECs invoke to make their claims for stranded cost recovery never existed. The guarantee of recovery that LECs claim is an ex post effort to recover assets and recoup actions for which management bears responsibility and for which stockholders have already been handsomely compensated.

There is now extensive documentation of uneconomic costs embedded in LEC operations that would not be recovered in a competitive marketplace and should not be recovered under any reasonable theory of economic regulation. These uneconomic costs include

- a persistent pattern of excess profits earned by the LECs, which has existed for a decade,
- inefficiencies in network provisioning and overhead costs, demonstrated in the FCC's proceedings on universal service and local competition, and
- a continuing misallocation of excessive investment in the network to access charges and local rates, demonstrated in the FCC's video dialtone cost allocation and Part 36 reform proceedings.

The LEC arguments also ignore the vast revenue opportunities that have been opened by the statute. They seek the competitive rewards of entry into new markets but also want to be protected from the risks of opening their own markets to competition.

Threats of court cases about confiscation are certainly not a basis for failing to implement the pro-competitive policy that Congress clearly had in mind when it passed the 1996 Act, especially when they fail virtually every test of current law and practice.

- Regulation was never intended to countenance inefficiency and the purpose of introducing competition is to eliminate it.
- Regulators never indemnified companies from technological obsolescence and have already compensated them for those risks.
- Far from guaranteeing complete recovery of all costs rendered uneconomic by competition, as LECs claim, current law places the burden of the risk of competition squarely on the shoulders of utilities. The risk premiums that LECs have earned already reflect handsome returns earned by incumbent local exchange companies.
- The extremely strong financial performance of local exchange companies undermines any claims that failure to recover obsolete and uneconomic investment will threaten the financial soundness of these companies.
- The balanced risk reward structure of the Telecommunications Act will certainly pass constitutional muster

Thus the legal, economic and regulatory basis for immediate action by the FCC on access charge reform is clear. There is no reason to delay billions of dollars of rate relief for consumers.

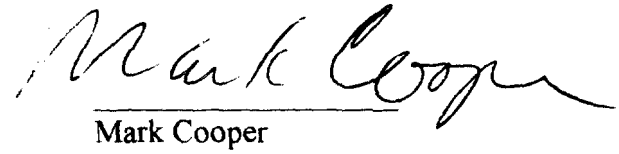
Respectfully submitted,

Gene Kimmelman
Co-Director, Washington Office
Consumers Union

Dr. Mark Cooper
Research Director
Consumer Federation of America

CERTIFICATE OF SERVICE

I, Mark cooper, do hereby certify that copies of the foregoing Reply Comments were sent via first class mail postage paid or hand delivery, to all parties of record on this 17th day of February, 1998.



Mark Cooper

Consumer Federation of America

# COMPETITION IN LOCAL TELEPHONE MARKETS:

# IS THE GLASS 98 PERCENT EMPTY OR 2 PERCENT FULL?

FEBRUARY 17, 1998

1424 16th Street, N.W., Suite 604 • Washington, D.C. 20036 • (202) 387-6121

Consumer Federation of America

# COMPETITION IN LOCAL TELEPHONE MARKETS: IS THE GLASS 98 PERCENT EMPTY OR 2 PERCENT FULL?

## EXECUTIVE SUMMARY

Based on recent evidence filed at the Federal Communications Commission and the Securities Exchange Commission, it is clear that rather than enjoying a vigorously competitive marketplace as the local exchange companies (LECs) claim, consumers still face a market that is monopolized by the incumbent LECs and immune to the market forces that would deliver the competitive benefits that the Telecommunications Act of 1996 promised. Two years after the passage of the Act, the LECs have demonstrated a remarkable ability to frustrate competition.

### THE CURRENT STATE OF COMPETITION

Any suggestion that the FCC can wait for developments in the marketplace to do the job of lowering prices to the efficient, forward looking levels that would prevail in a competitive marketplace has been laid to rest by year-end 1997 evidence on the state of competition (see Table ES-1).

- Even if we accept their overblown claims about business "lost" to competitors, the four LECs who have made data available retain a 98 percent market share.

- Moreover, the LEC share of facilities-based competition, which is all that counts for access charge reform and in the long run what counts in the marketplace, is even higher, over 99 percent.

- Finally, it turns out that LECs have not even "lost" anything. For all the complaining about competitive incursions into their business, the Baby Bells have added over four times as many lines as competitors since the passage of the 1996 Telecom Act.

- Many claim to have added lines and revenues at record levels in 1997.



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TABLE ES-1:
LEC CLAIMS OF LOCAL COMPETITION IN PERSPECTIVE

| | LEC LINES (000000) 1997 | ADDED '96&'97 | CLEC LINES (000000) 1997 | % RESALE | CLEC MARKET SHARE (%) ALL | FACILITIES |
|---|---|---|---|---|---|---|
| AMERITECH | 20.5 | 1.4 | .6 | 82 | 3.0 | .5 |
| BELL ATLANTIC a/ | 39.7 | 2.7 | .7 | 31 | 1.8 | 1.1 |
| BELL SOUTH | 23.2 | 2.1 | .2 | 95 | 1.0 | .1 |
| S.C. b/ | 33.1 | 3.1 | .6 | 56 | 1.8 | .7 |
| 4 LEC TOTAL | 116.5 | 9.3 | 2.1 | 59 | 1.8 | .7 |

SOURCE: Competitive LEC data is from January 30, 1998 comments filed in In the Matter of Consumer Federation of America, International Communications Association and National Retail Federation Petition Requesting Amendment of the Commission's Rules Regarding Access Charge Reform and Price Cap Performance Review for Local Exchange Carriers, Docket No. RM9210 -- Ameritech Attachment C; Bell Atlantic, pp. 6, 10, and Attachment 1; BellSouth, p. 5; S.C., Attachment; U.S. Telephone Association, pp. 7-8 and Attachment, pp. 22-23. Bell Atlantic's total is reiterated in Dee May, Competition Progress Report, February 2, 1998. Year-end 1997 LEC lines are from LEC final quarter press releases -- Ameritech, Ameritech Earnings Per Share Up 12% in Forth Quarter and Year, Before One-time Items; Fifth Consecutive Year of Double-Digit Growth, January 13, 1998; Bell Atlantic, Bell Atlantic Announces Third Consecutive Year of Double-Digit Earnings Growth, n.d.; BellSouth, Bell South Reports Fifth Year of Earnings Growth, Increase in Access Lines Sets Fourth Annual Record in Row; Wireless Customers Worldwide Surpass 6 Million, January 22, 1998; S.C., S.C. Delivers Strong 1997 Performance; Growth in Core Businesses, Merger Success Highlight Year, January 28, 1998.

a/ Bell Atlantic's claim for total facilities bypass seems high in light of the New York PSC analysis of facilities based competition, but the claimed number is included.

b/ Assumes the same proportion of resale as in August 1997, per USTA, Attachment p. 23.

In the new era of common sense regulation advocated by the Commission, perhaps the most bedrock common sense notion that Americans have about their marketplace economy is that companies with a 95 or 98 or 99 percent market share do not face effective competition.

## PROSPECTS FOR COMPETITION

The simple, inescapable fact is that the regulatory structure that the FCC had hoped would foster competition under the 1996 Act has been severely damaged, if not destroyed, by the unrelenting resistance of LECs to local competition in the courts, the marketplace, and the regulatory arena. Since the FCC acted in the access reform docket, the market opening process has suffered a series of major setbacks.

- FCC's pricing rules vacated, cost-based UNE pricing reopened in many states by the 8th Circuit ruling; FCC's section 251 role restricted, scope of the FCC's 271 review limited, Ubundled Network Elements platform undermined by the 8th Circuit's recombination ruling; the LEC refusal to provide shared transport, RBOC restrictions invalidated, Number Portability implementation schedule delayed, Operational Support Systems have failed to develop, section 271 applications have become weaker, not stronger, section 271 found unconstitutional by a lower court (see Table ES-2).

TABLE ES-2
THE LITIGATION MINEFIELD CREATED SINCE THE
INITIAL FEDERAL COMMUNICATIONS COMMISSION DECISION
ON ACCESS CHARGE REFORM

| ISSUE | COURT CASE |
|---|---|
| Pricing Authority | Iowa Utilities Board v. FCC (8th Cir. 96-3321, Jul. 18, 1997) |
| Recombination | Iowa Utilities Board v. FCC (8th Cir. 96-3321, Oct. 14, 1997) |
| Access Charge Reform | S.C. v. FCC (8th Cir. 97-2618) |
| Shared Transport | S.C. v. FCC (8th Cir. 97-3389) |
| Non-Accounting Safeguards | Bell Atlantic v. FCC. (D.C. Cir. 97-1432) |
| Local Number Portability | US West v. FCC (10 Cir. 97-9518) |
| 271 Decision Challenges | BellSouth v. FCC (D.C. Cir 98- ) |
| Pricing in 271 cases | Iowa Utilities Board v. FCC (8th Cir. 96-3321, Jan. 22, 1998) |
| 271 Constitutionality | S.C. v. FCC (Civil No. 7-97-CV-163-X, Dec. 31, 1997) |
| Cost-Based Pricing | GTE California Inc. V. Conlon (C-97-1756), Southwestern Bell Tel. Co. v. AT&T Communications, Inc. (Texas, No. A-97-CA-132-SS) |
| Arbitration Reopeners | US WEST Communications, Inc. v. Thoms (No. 4-97-CV-70082) |
| Delay of Orders | US WEST Communications, Inc. v. Hix (Colorado, No. 97-D-152) US WEST Communications, Inc. v. Garvey (Minnesota, No. 97-913), US WEST Communications v. Thoms (South Dakota, No. 4-97-CV-70082), Bell Atlantic-Delaware v. McMahon (Delaware, No. 97-312). |

SOURCE: Complied from January 30, 1998 comments filed in In the Matter of Consumer Federation of America, International Communications Association and National Retail Federation Petition Requesting Amendment of the Commission's Rules Regarding Access Charge Reform and Price Cap Performance Review for Local Exchange Carriers, Docket No. RM9210

It is ironic and troubling to hear corporate officers claim that their fiduciary

responsibility to stockholders requires them to participate in the law suits seeking to overturn the Act, but they really want to comply with it. It is clear that their overarching responsibility is to defending their monopoly revenues as best they can.

We believe that the FCC has a fiduciary responsibility to the public, to lower prices it has repeatedly and loudly proclaimed are above cost, uneconomic and incompatible with a competitive marketplace. The regulatory agency charged with protecting the public must be just as vigorous in its defense of the public interest as the corporation have been in defense of their private interests. The only way that the FCC can immediately and effectively do that is to lower access charges.

## THE LEGAL BASIS OF ACCESS CHARGE REFORM

Whenever the LECs are confronted with the prospect of having their revenue streams reduced, no matter what proceeding at the state or federal level, they insist that their constitutional rights of property are about to be violated.

- Since this legal challenge is inevitable, we urge the FCC to take aggressive action to lower consumers bills now and defend that decision in the courts. Put the money in the people's pockets and let the LECs try to take it out through court cases. We are convinced they will fail and that state and federal regulators should not delay competition over the issue of embedded costs.

The version of the regulatory compact between stockholders and ratepayers that LECs invoke to make their claims for stranded cost recovery never existed.

There is now extensive documentation of uneconomic costs embedded in LEC operations that would not be recovered in a competitive marketplace and should not be recovered under any reasonable theory of economic regulation. These uneconomic costs include

- a persistent pattern of excess profits earned by the LECs, which has existed for a decade, inefficiencies in network provisioning and overhead costs, demonstrated in the FCC's proceedings on universal service and local competition, and a continuing misallocation of excessive investment in the network to access charges and local rates, demonstrated in the FCC's video dialtone cost allocation and Part 36 reform proceedings.

The LEC arguments also ignore the vast revenue opportunities that have been

opened by the statute. They seek the competitive rewards of entry into new markets but also want to be protected from the risks of opening their own markets to competition.

Threats of court cases about confiscation are certainly not a basis for failing to implement the pro-competitive policy that Congress clearly had in mind when it passed the 1996 Act, especially when they fail virtually every test of current law and practice.

- Regulation was never intended to countenance inefficiency and the purpose of introducing competition is to eliminate it.

- Regulators never indemnified companies from technological obsolescence and have already compensated them for those risks.

- Far from guaranteeing complete recovery of all costs rendered uneconomic by competition, as LECs claim, current law places the burden of the risk of competition squarely on the shoulders of utilities. The risk premiums that LECs have earned already reflect handsome returns earned by incumbent local exchange companies.

- The extremely strong financial performance of local exchange companies undermines any claims that failure to recover obsolete and uneconomic investment will threaten the financial soundness of these companies.

- The balanced risk reward structure of the Telecommunications Act will certainly pass constitutional muster

It is clear beyond any doubt that the consuming public would benefit from an immediate reduction in access charges and that competition in the telecommunications industry will not get started without immediate reform of access charges. As long as the local exchange companies (LECs) enjoy billions of dollars of monopoly profits and pricing rules that protect their excess profits, inefficiencies and strategically misallocated costs, their primary corporate interest will be to prevent competitors from entering the market to threaten those revenues. Thus the legal, economic and regulatory basis for immediate action by the FCC on access charge reform is clear. There is no reason to delay billions of dollars of rate relief for consumers.

# DELIVERING THE PROMISE OF THE TELECOMMUNICATIONS ACT of 1996

The recent petition filed by the Consumer Federation of America[1] seeking immediate relief from excessive access charges imposed by local exchange companies could result in price reductions to consumers of billions of dollars. The petition has been broadly supported by consumer groups representing all classes of customers.[2]

Not surprisingly, the local exchange companies (LECs) have urged the Federal Communications Commission (FCC) to reject the petition on factual, procedural and legal grounds. The factual reason that the LECs offer is the claim that competition is developing rapidly and is adequate to discipline pricing of access service. The procedural reason they give is that nothing has changed to cause the FCC to reopen its access charge decision of a year ago. The legal reason they give is that a reduction in access charges would constitute a taking of their property and is unconstitutional.

The LEC arguments are wrong. Of utmost importance for consumers and policy makers, they ignore the reality of the marketplace.

- Rather than enjoying a vigorously competitive marketplace as the LECs claim, consumers still face a LEC monopoly that is immune to the market forces that would deliver the benefits that the Telecommunications Act of 1996 promised.

This report documents the dismal state of local competition. As has been CFA's practice in its analysis of local markets, the report does not rely on any evidence from potential competitors of the local exchange carriers. It cites only other consumer groups (all of whom have filed in support of the petition) and the LEC provided data.

Based on the evidence in this proceeding, it is clear beyond any doubt that the consuming public would benefit from an immediate reduction in access charges and that competition in the telecommunications industry will not get started without

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[1]CFA's petition has been docketed in Federal Communications Commission, In the Matter of Consumer Federation of America, International Communications Association and National Retail Federation Petition Requesting Amendment of the Commission's Rules Regarding Access Charge Reform and Price Cap Performance Review for Local Exchange Carriers, Docket No. RM9210.

[2]In addition to the original petitioners, International Communications Association and the National Retail Federation, the Commission has now heard from Consumers Union, the Ad Hoc Telecommunications Users Group and the American Petroleum Institute.

immediate reform of access charges. As long as the local exchange companies enjoy billions of dollars of monopoly profits and pricing rules that protect their excess profits, inefficiencies and strategically misallocated costs, their primary corporate interest will be to prevent competitors from entering the market to threaten those revenues. Two years after the passage of the Telecommunications Act of 1996, they have demonstrated a remarkable ability to frustrate competition. Any suggestion that the FCC can wait for developments in the marketplace to do the job of lowering access charges to the efficient, forward looking levels that would prevail in a competitive marketplace has been laid to rest by the evidence in this proceeding.

## THE ACTUAL STATE OF LOCAL COMPETITION

In their filings the LECs have provided evidence on the status of competition in the local market. It does not present a pretty picture two years after the passage of the 1996 Act.[3]

Even if we accept their overblown claims about business "lost" to competitors, the four LECs who have made data available retain a 98 percent market share. Table 1 shows that the 4 LECs who have provided data, representing approximately three-quarters of all lines in the nation, and certainly those where the greatest competition exists have lost only 1.8 percent of the local lines to competitors.

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[3]The American Petroleum Institute, "Comments in Support of Petition for Rulemaking," Docket Rm-9210, January 30, 1998 (hereafter API), p. 8, concludes as follows:

> Consumers have yet to see the emergence of "workable competition" in local telecommunications markets or to realize the promises of greater choice and lower rates. In fact, end-users -- particularly multiline business line end-users -- are seeing *substantial rate increases* attributable to new presubscribed interexchange carrier charges (PICCs) and universal service surcharges and, in some instances, increased subscriber line charges (SLCs).
>
> High end-user rates confirm that local competition has failed to develop as the Commission anticipated. If workable competition were beginning to emerge, disgruntled end-users could avoid the new PICCs and increased SLCs by purchasing their local and long-distance telecommunications service from a competitive local exchange carrier (CLEC). Due to the paucity of competitive options, whoever, such movement is not occurring.
>
> Because legal, economic, and operational barriers to local entry remain largely intact, the "market forces" operating in access markets today and for the near terms are primarily those associated with monopoly markets. In these markets, rates have been set and remain far above cost. These grossly-inflated access rates directly penalize end-users, since the incumbents generate their monopoly profits from customers purchasing services in the competitive long distance market. As long as the incumbents retain their monopoly grip on access services, as well as the network functions used to provide access, access rates will not move toward economic costs.

TABLE 1:
LEC CLAIMS OF LOCAL COMPETITION IN PERSPECTIVE

| | LEC LINES (000000) | CLEC LINES (000000) | CLEC MARKET SHARE (%) |
|---|---|---|---|
| AMERITECH | 20.5 | .6 | 3.0 |
| BELL ATLANTIC | 39.7 | .7 | 1.8 |
| BELL SOUTH | 23.2 | .2 | 1.0 |
| SBC | 33.1 | .6 | 1.8 |
| 4 LEC TOTAL | 116.5 | 2.1 | 1.8 |

SOURCE: Competitive LEC data is from January 30, 1998 comments filed in In the Matter of Consumer Federation of America, International Communications Association and National Retail Federation Petition Requesting Amendment of the Commission's Rules Regarding Access Charge Reform and Price Cap Performance Review for Local Exchange Carriers, Docket No. RM9210 -- Ameritech Attachment C; Bell Atlantic, pp. 6, 10, and Attachment 1; BellSouth, p. 5; SBC, Attachment; U.S. Telephone Association, pp. 7-8 and Attachment, pp. 22-23. Bell Atlantic's total is reiterated in Dee May, Competition Progress Report, February 2, 1998. Year-end 1997 LEC lines are from LEC final quarter press releases -- Ameritech, Ameritech Earnings Per Share Up 12% in Forth Quarter and Year, Before One-time Items; Fifth Consecutive Year of Double-Digit Growth, January 13, 1998; Bell Atlantic, Bell Atlantic Announces Third Consecutive Year of Double-Digit Earnings Growth, n.d.; BellSouth, Bell South Reports Fifth Year of Earnings Growth, Increase in Access Lines Sets Fourth Annual Record in Row; Wireless Customers Worldwide Surpass 6 Million, January 22, 1998; SBC, SBC Delivers Strong 1997 Performance; Growth in Core Businesses, Merger Success Highlight Year, January 28, 1998.

Moreover, the LEC share of facilities-based competition, which is all that counts for access charge reform[4] and in the long run what counts in the marketplace,[5] is even higher. Table 2 shows that for the four LECs who have provided data,

[4]The FCC allows the LECs to retain access revenue on resold local service. Therefore, only facilities-based competition or a combination of facilities and unbundled elements can place downward pressure on access charges. Pure resale cannot affect access charges. Moreover, CFA has demonstrated that resale does not provide effective competition for local service (see Stonewalling Local Competition: The Baby Bell Strategy to Subvert the Telecommunications Act of 1996, January 6, 1998).

[5]So long as competitors are dependent on incumbents for a slightly discounted version of the incumbent offering, the cannot be effective price competitors of the incumbents.

approximately 60 percent of the lines "lost" to competitors have been "lost" through resale, not facilities based competition. Consequently, the LEC market share of facilities-based competition is over 99 percent.

TABLE 2
THE ROLE OF RESALE IN LOCAL COMPETITION

| | CLEC LINES (000) | RESOLD LINES | % RESALE |
|---|---|---|---|
| AMERITECH | 600 | 489 | 82 |
| BELL ATLANTIC a/ | 720 | 220 | 31 |
| BELL SOUTH | 230 | 218 | 95 |
| SBC b/ | 560 | 314 | 56 |
| 4 LEC TOTAL | 2110 | 1241 | 59 |

SOURCE: Competitive LEC data is from January 30, 1998 comments filed in In the Matter of Consumer Federation of America, International Communications Association and National Retail Federation Petition Requesting Amendment of the Commission's Rules Regarding Access Charge Reform and Price Cap Performance Review for Local Exchange Carriers, Docket No. RM9210 -- Ameritech Attachment C; Bell Atlantic, pp. 6, 10, and Attachment 1; BellSouth, p. 5; SBC, Attachment; U.S. Telephone Association, pp. 7-8, Attachment A, pp. 22-23.. Bell Atlantic's total is reiterated in Dee May, Competition Progress Report, February 2, 1998.

a/ Bell Atlantic's claim for total facilities bypass seems high in light of the New York PSC analysis of facilities based competition, but the claimed number is included.

b/ Assumes the same proportion of resale as in August 1997, per USTA, Attachment p. 23.

It turns out that LECs have not even "lost" anything. For all the complaining about competitive incursions into their business, the Baby Bells have added over four times as many lines as competitors since the passage of the 1996 Telecom Act. Table 3 shows the growth of lines enjoyed by the LECs for whom data is available on

competition. Several of the source documents claim that the growth in access lines and revenues in 1997 set records, laying to rest claims that LECs are being hurt by competition.

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TABLE 3:
ADDITIONAL LINES SERVED SINCE THE PASSAGE OF THE TELECOMMUNICATIONS ACT OF 1996

LINES ADDED IN 1996 AND 1997

| | LEC LINES (000000) | CLEC LINES (000000) |
|---|---|---|
| AMERITECH | 1.4 | .6 |
| BELL ATLANTIC | 2.7 | .7 |
| BELL SOUTH | 2.1 | .2 |
| SBC | 3.1 | .6 |
| 4 LEC TOTAL | 9.3 | 2.1 |

SOURCE: Competitive LEC data is from January 30, 1998 comments filed in In the Matter of Consumer Federation of America, International Communications Association and National Retail Federation Petition Requesting Amendment of the Commission's Rules Regarding Access Charge Reform and Price Cap Performance Review for Local Exchange Carriers, Docket No. RM9210 -- Ameritech Attachment C; Bell Atlantic, pp. 6, 10, and Attachment 1; BellSouth, p. 5; SBC, Attachment; U.S. Telephone Association, pp. 7-8, Attachment. Bell Atlantic's total is reiterated in Dee May, Competition Progress Report, February 2, 1998. Year-end 1997 LEC lines are from LEC final quarter press releases -- Ameritech, Ameritech Earnings Per Share Up 12% in Forth Quarter and Year, Before One-time Items; Fifth Consecutive Year of Double-Digit Growth, January 13, 1998; Bell Atlantic, Bell Atlantic Announces Third Consecutive Year of Double-Digit Earnings Growth, n.d.; BellSouth, Bell South Reports Fifth Year of Earnings Growth, Increase in Access Lines Sets Fourth Annual Record in Row; Wireless Customers Worldwide Surpass 6 Million, January 22, 1998; SBC, SBC Delivers Strong 1997 Performance; Growth in Core Businesses, Merger Success Highlight Year, January 28, 1998. LEC Lines at year end 1996 are from Federal Communications Commission, Statistics of Common Carriers: 1996/1997, Table 1.

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Even in the most competitive market segment of the most competitive geographic market -- business customers in New York City -- the incumbent still

retains a 95 percent market share of facilities-based service. In the residential market, the absolute monopoly of the incumbent remains virtually untouched, Table 4 shows the extent of facilities-based competition in New York State, as analyzed by the state Public Service Commission. There is virtually no facilities-based competition for residential service anywhere in the state, and little for business customers outside of the New York City area.

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TABLE 4
THE CONCENTRATION OF FACILITIES-BASED
LOCAL COMPETITION IN NEW YORK

COMPETITOR FACILITIES BASED MARKET SHARE

| | METRO NEW YORK | UPSTATE | TOTAL |
|---|---|---|---|
| RESIDENTIAL | .1 | 0 | 0 |
| BUSINESS | 4.7 | 1.1 | 4.0 |
| TOTAL | 1.8 | .3 | 1.4 |

Source: Competitive LEC data is from January 30, 1998 comments filed in In the Matter of Consumer Federation of America, International Communications Association and National Retail Federation Petition Requesting Amendment of the Commission's Rules Regarding Access Charge Reform and Price Cap Performance Review for Local Exchange Carriers, Docket No. RM9210 -- Bell Atlantic, Attachment 1.

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In the new era of common sense regulation advocated by the Commission, perhaps the most bedrock common sense notion that Americans have about their marketplace economy is that companies with a 95, 98 or 99 percent market share do not face effective competition. This common sense notion is supported by decades of economic research. Theories that the mere threat of competition is adequate to accomplish the same outcome as a truly competitive market have been disproven and rejected.

Moreover, it should be noted that the FCC's evaluation of competition for purposes of access charge reform is not constrained by the facilities-based competition or "competitive checklist" language in section 271 of the Telecommunications Act. It can apply a common sense notion of competition to access charge reform more akin to the traditional public interest review. It can look at the lack of geographic spread of competition; it can look at the overwhelming market share of the incumbents and conclude that competition is not now adequate to force access prices down and is not likely to be so in the foreseeable future.

## THE PROCEDURAL STATUS OF MARKET OPENING

A second reason that the LECs claim CFA's petition should be rejected is that nothing has changed to cause the Commission to reopen its access charge order. The LECs ignore the fact that the FCC has now been forced to conclude in several section 271 proceedings that competition has not developed sufficiently in a number of additional states, while court rulings have made it more difficult for competitors to enter the market

The prospects for widespread local competition that can place downward pressures on access charges are bleak and have suffered major setbacks in recent months. The simple, inescapable fact is that the regulatory structure that the FCC had hoped would foster competition under the 1996 Act has been severely damaged, if not destroyed, by the unrelenting resistance of LECs to local competition in the courts, the marketplace, and the regulatory arena.

Since the FCC acted in the access reform docket, the market opening process has suffered a series of major setbacks including

- FCC's pricing rules vacated,
- cost-based UNE pricing reopened in many states by the 8th Circuit ruling,
- FCC's section 251 role restricted,
- scope of the FCC's 271 review limited,
- UNE platform undermined by the 8th Circuit's recombination ruling

- o the LEC refusal to provide shared transport,
- o RBOC restrictions invalidated,
- o Number Portability implementation schedule delayed,
- o Operational Support Systems failed to develop,
- o section 271 applications became weaker, not stronger,
- o section 271 found unconstitutional by a lower court.[6]

Table 5 lists the cases cited to the Commission in the comments filed in this proceeding which have sought to over turn or delay procompetitive decisions by regulatory commissions at the state and federal level. While the major strategies for obstructing local competition are identified in the Table, there are dozens, if not hundreds more specific legal and regulatory maneuvers of a similar ilk not identified on the list.

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[6]API, pp. 7-8, summarizes the developments as follows:

In the months since release of the *Access Charge Reform Order*, events have given lie to the Commission's confident pronouncements. Numerous appellate setbacks have gutted the Commission's efforts to dismantle the legal and economic barriers to entry in local markets. Highlights include:

- o Pricing Rules Vacated...
- o FCC's Section 251 Role Restricted...
- o UNE Platform in Disarray...
- o RBOC Restrictions Invalidated...
- o Scope of FCC's 271 Review Limited...
- o Number Portability: extended its implementation schedule
- o Operational Support Systems (OSS): after deadline

TABLE 5

THE LITIGATION MINEFIELD CREATED SINCE THE INITIAL FEDERAL COMMUNICATIONS COMMISSION DECISION ON ACCESS CHARGE REFORM

| ISSUE | COURT CASE |
|---|---|
| Pricing Authority | Iowa Utilities Board v. FCC (8th Cir. 96-3321, Jul. 18, 1997) |
| Recombination | Iowa Utilities Board v. FCC (8th Cir. 96-3321, Oct. 14, 1997) |
| Access Charge Reform | SBC v. FCC (8th Cir. 97-2618) |
| Shared Transport | SBC v. FCC (8th Cir. 97-3389) |
| Non-Accounting Safeguards | Bell Atlantic v. FCC. (D.C. Cir. 97-1432) |
| Local Number Portability | US West v. FCC (10 Cir. 97-9518) |
| 271 Decision Challenges | BellSouth v. FCC (D.C. Cir 98- ) |
| Pricing in 271 cases | Iowa Utilities Board v. FCC (8th Cir. 96-3321, Jan. 22, 1998) |
| 271 Constitutionality | SBC v. FCC (Civil No. 7-97-CV-163-X, Dec. 31, 1997) |
| Cost-Based Pricing | GTE California Inc. V. Conlon (C-97-1756), Southwestern Bell Tel. Co. v. AT&T Communications, Inc. (Texas, No. A-97-CA- 132-SS) |
| Arbitration Reopeners | US WEST Communications, Inc. v. Thoms (No. 4-97-CV-70082) |
| Delay of Orders | US WEST Communications, Inc. v. Hix (Colorado, No. 97-D-152) US WEST Communications, Inc. v. Garvey (Minnesota, No. 97-913), US WEST Communications v. Thoms (South Dakota, No. 4-97-CV-70082), Bell Atlantic-Delaware v. McMahon (Delaware, No. 97-312). |

Applications for section 271 relief are getting worse, not better.[7] Whereas Ameritech Michigan failed five of the check-list items, BellSouth South Carolina failed at least nine and BellSouth Louisiana failed as many as twelve.

As a result of court decisions, competitors have no idea of the terms and conditions under which they will be allowed to combine network elements to commence facilities-based competition. Under cross examination LECs have been forced to admit that recent court rulings have completely scrambled the business plans of new entrants. In New York,[8] for example, Bell Atlantic admitted that close

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[7]See Reply Comments of the Consumer Federation of America," before the Federal Communications Commission, In the Matter of Application by Bell South Corporation, et. Al. For Provision of In-Region, InterLATA Services in South Carolina, CC Docket No. 97-208, November 14, 1997; In the Matter of Application by Bell South Corporation, Bell South Telecommunications, Inc., and BellSouth Long Distance, Inc., for Provision of In-Region, InterLATA Services in Louisiana, CC Docket No. 97-231, December 18, 1997.

[8]"Minutes of Technical Conference," Petition of New York Telephone Company for Approval of its Statement of Generally Available Terms and Conditions Pursuant to Section 252 of the Telecommunications Act of 1996 and Draft Filing on Petition for InterLATA Entry Pursuant to Section 271 of the Telecommunications Act of 1996, Case 97-C-0271 New York State Public Service Commission

> (Bell Atlantic witness Goldberg, p. 1296). Well, our policy is to require either physical or virtual collocation be used to connect any unbundled elements. I'm not completely sure of the dates, but we have tariffs in effect in New York which I believe we filed modifications to conform them to that policy which reflects the 8th Circuit Court decision and I don't recall offhand what the current proposed effective date of those tariffs is.
>
> I believe it is some time in January, so as of that date, if that's the date the tariff changes become effective, the effect of those tariff changes would require collocation to make that connection then from that point on that would be the mode of connecting unbundled elements.
>
> (Staff Counsel, p. 1298) Does Bell Atlantic require collocation for access to interoffice transmission facilities as and unbundled element?
>
> (Bell Atlantic Witness Calabro) Yes.
>
> And does Bell Atlantic require collocation for access to signaling networks and call-related databases as unbundled network elements.?
>
> Yes.
>
> And is collocation required for access to operator services and directory assistance?
> As an unbundled network element, it is, and in fact there's no way to gain access to unbundled network elements, facilities or equipments or the functionalities embodied in those facilities equipment without collocation.
>
> (Bell Atlantic Witness, Smith pp. 999-1000) The assumptions that we had made regarding the 8th Circuit decision in October was that some of the demand that we would have seen for combination of unbundled network elements would move to resale.

to 70 percent of the lines that competitors had planned to provision with unbundled network elements would have to be reconfigured as a result of the Eighth Circuit Court Ruling on recombination of network elements, To put the matter simply, this sets facilities-based competition back at least a year.[9]

Moreover, although the ruling in a Wichita Falls Federal District Court, which declared section 271 unconstitutional, has been stayed, it casts a dark shadow over the market opening process. The commitment of the LECs to complying with section 271 of the law is subject to serious doubt. The companies that led the charge in attacking the statute have said different things in different courts -- professing to accept and support section 271 before some courts and regulatory commission while simultaneously challenging it in others. Even the companies who have claimed to be most committed to opening their markets jumped on the bandwagon that sought to overturn the statute. The commitment of the RBOCs to complying with section 271 and opening their markets is questionable at best.

CFA finds it ironic and troubling to hear corporate officers claim that their fiduciary responsibility to stockholders required them to participate in the law suits seeking to overturn the Act, but they really want to comply with it. It is clear that their primary responsibility is to defending their monopoly revenues as best they can.

We believe that the FCC has a fiduciary responsibility to the public, to lower prices it has repeatedly and loudly declared are above costs, uneconomic and incompatible with a competitive marketplace. The regulatory agency charged with protecting the public must be just as vigorous in its defense of the public interest as the corporation have been in defense of their private interests.

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> Another portion would move to loops only where somebody would deploy their own switch and by loops we mean there were some that might potentially move, although we did not see much into a real strict bypass situation...
>
> In 1998 we had actually forecast by quarter and then we had assumed that in the first quarter of 1998 the demand for combined elements would move 85 percent to resale lines, 10 percent to a link and a port that would be combined by the carrier using collocation and 5 percent a link only.
>
> In the second quarter we are looking at percentages of 80, 15, 5... By the third quarter 65..25..10 and fourth quarter 40..45..15.

[9]For a discussion of these and other issues in New York, see "Initial Brief of the Consumer Federation of America," Petition of New York Telephone Company for Approval of its Statement of Generally Available Terms and Conditions Pursuant to Section 252 of the Telecommunications Act of 1996 and Draft Filing on Petition for InterLATA Entry Pursuant to Section 271 of the Telecommunications Act of 1996, Case 97-C-0271, New York State Public Service Commission, January 6, 1998.

While CFA has encouraged and supported the FCC in its efforts to open markets under the 1996 Act and we continue to do so, access charge reform is not dependent on the 1996 Act. It need not, and, in light of the actions of the LECs who are resisting opening their markets are every turn, it should not wait for competition to succeed or fail under the Act.[10] Access charge reform should begin now.

## THE LEGAL BASIS OF ACCESS CHARGE REFORM

Whenever the LECs are confronted with the prospect of having their revenue streams reduced, no matter what proceeding at the state or federal level, they insist that their constitutional rights of property are about to be violated.[11]

- Since this legal challenge is inevitable, we urge the FCC to take aggressive action to lower consumers bills now and defend that decision in the courts. Put the money in the people's pockets and let the LECs try to take it out through court cases. We are convinced they will fail and that state and federal regulators should not allow embedded costs to stand in the way of competition.

The version of the regulatory compact between stockholders and ratepayers that LECs invoke to make their claims for stranded cost recovery never existed. The guarantee of recovery that LECs claim is an ex post effort to recover assets and recoup actions for which management bears responsibility and stockholders have already been handsomely compensated.

To compensate companies for uneconomic investments, when they have already been compensated for the risk of those investments, constitutes a double

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[10]Ad Hoc, p. 2, points out

> If access service pricing based on forward-looking incremental costs is appropriate for ILEC services facing competition, the Commission should also require such pricing for non-competitive services. As long as ILEC costs are common to competitive and non-competitive services, the Commission should set rates for the competitive and non-competitive services based on TSLRIC. The TSLRIC of providing access service should not be materially different, if at all different, from the TELRIC of providing UNEs. Thus, while the Commission's jurisdiction to require TELRIC-based pricing of UNEs may be under a cloud, the Commission certainly has jurisdiction over the pricing of interstate access service. If the Commission believe that state public utility authorities should price UNEs based on TELRIC, it should accept responsibility to set interstate access service rates based on TSLRIC.

[11]This claim has been made in every proceeding since the passage of the Act and is reiterated by the LECs in this proceeding.